DIRECT TESTIMONY OF

JIMMY E. ADDISON

ON BEHALF OF

SOUTH CAROLINA ELECTRIC & GAS COMPANY

DOCKET NO. 2007-229-E

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND POSITION.

A. My name is Jimmy E. Addison and my business address is 1426 Main Street, Columbia, South Carolina. I am Senior Vice President and Chief Financial Officer of South Carolina Electric & Gas Company ("SCE&G" or the "Company") and hold a similar position at SCANA Corporation, which is the parent company of SCE&G.

Q. PLEASE DESCRIBE YOUR EDUCATION AND BUSINESS BACKGROUND.

A. I am a graduate of the University of South Carolina with a Bachelor of Science Degree in Business Administration, majoring in accounting, and a Master of Accountancy Degree. Also, I am a Certified Public Accountant in South Carolina. Prior to my employment by the Company in March 1991, I was employed for seven years by the public accounting firm of Deloitte & Touche, where I was designated an Audit Manager as a public utility accounting and audit specialist. I was also a partner in the public accounting firm of Hughes, Boan and Addison immediately prior to joining the Company in 1991.

Q. WHAT ARE YOUR DUTIES WITH SCE&G?

A. As Senior Vice President and Chief Financial Officer of SCE&G, I have responsibility for monitoring the Company's present and prospective financial condition; for formulating strategies to ensure that the Company can meet its capital requirements at the lowest reasonable cost; and for managing all accounting and financial matters related to the Company. In that regard, I meet regularly with members of the financial community, including the Wall Street analysts and credit rating agency personnel who follow the electric utility industry in general and SCE&G specifically. In these meetings, we discuss their perceptions and concerns about the Company, its financial and business position, the capital markets and the utility industry generally. We also discuss the various risk factors that the Company faces as seen by investors. I am also regularly involved in discussions of investors' perspectives on the Company with underwriters and other experts as such views pertain to the issuance or refinancing of debt and the issuance of new common stock.

Q. HAVE YOU EVER TESTIFIED BEFORE THIS COMMISSION?

A. Yes. I have testified in numerous proceedings before this Commission.

Q. PLEASE PROVIDE THE COMMISSION WITH A FINANCIAL OVERVIEW OF SCE&G'S RATE INCREASE REQUEST IN THIS

PROCEEDING.

A. The test period in SCE&G's last electric rate proceeding, Docket 2004-178-E, closed on March 31, 2004. Since that time, SCE&G has spent a total of $786 million in capital on its electric generation, transmission and distribution system. That capital has been spent for such things as system expansion to serve new customers, reliability upgrades to the transmission and distribution system, environmental upgrades to generation plants, and capital maintenance. The impact of these capital expenditures, along with increases in operating and maintenance costs, depreciation expenses, taxes, and other items, have reduced the Company's pro-forma return on common equity to 8.27%. As I discuss later in my testimony, considering today's capital markets and the Company's current risk profile, the appropriate return on equity for the Company is 11.75%. Therefore, the Company is seeking an increase in its retail electric rates of $118 million based on a test year ended March 31, 2007.

Q. IS IT POSSIBLE TO IDENTIFY THE CHANGES IN THE COMPANY'S FINANCES THAT HAVE RESULTED IN THE NEED FOR RATE ADJUSTMENTS AT THIS TIME?

A. Yes. But it is important to recognize that many hundreds of expense, capital and revenue items are netted together to determine the Company's financial results in each period. These expense, capital and revenue items can vary in opposing directions and can change in offsetting or compounding ways. As a result, an accurate view of how the Company's revenue and expense profile is changing cannot be gained by viewing any single component or group of components in isolation.

However, I can identify some of the principal changes in the Company's financial profile since the 2004 rate proceeding that have resulted in the need for the rate adjustments presented in this case.

Q. PLEASE EXPLAIN WHAT YOU MEAN BY THE OFFSETTING OR INTERACTION AMONG CAPITAL, EXPENSE OR REVENUE COMPONENTS.

A. Certainly. Service to new customers may result in additional revenues. But additional capital costs and expenses (more investments in lines and plants, more personnel to support operations, more billing costs, etc.) are involved in providing the service. These additional capital costs and expenses may offset some or all of the revenue gains. Investments in assets that improve employee productivity or plant efficiency, but reduce labor costs or fuel costs, increase capital expenses, maintenance costs, property taxes, depreciation, and insurance. Depreciation expense lowers returns, but also reduces net plant in service, which reduces capital costs.

In measuring financial performance, all of these changes in revenues and expenses are netted against each other. Comparisons of changes in individual items rarely present an accurate or complete picture of how the expense and revenue financial profile of the company is changing.

Q. WHAT COST COMPONENTS DO YOU SEE AS IMPORTANT FOR UNDERSTANDING THE PRESENT RATE FILING?

A. An important component of cost underlying this case is the Company's increased levels of ongoing investment in capital assets, principally in transmission and distribution assets and in generation plant. As mentioned above, in the three years since the last retail rate case, the Company has invested a total of $786 million in new generation, transmission and distribution assets. As Mr. Marsh has explained in his direct testimony, this investment has not been characterized by investment in any single plant or project. Instead, it consists of investment in a broad range of capital projects required to extend service to new customers, to strengthen the ability of SCE&G's transmission and distribution system to meet increasing demand, to overcome the effects of wear-and-tear on generation, transmission and distribution assets, and to allow generating plants to meet increasingly stringent environmental regulations.

During this same three-year period, depreciation of generation, transmission and distribution plant has offset $500 million of this new investment, resulting in a net increase in generation, transmission, and distribution plant of $286 million. The additional annual revenue requirement associated with this increased net generation, transmission and distribution rate base is approximately $38 million based on the weighted average cost of capital contained in the Application.

In a similar vein, SCE&G has been required to purchase SO_2 allowances related to its fossil fuel plant operations to comply with environmental regulations. These allowances are held in fuel inventory. In addition, coal and oil prices –which affect the value of inventory—have increased as has the size of coal inventories. For all these reasons, the value of fuel inventory has increased by $90 million since the last rate proceeding. This additional fuel inventory cost adds $12 million to the Company's revenue requirement in this case.

Also related to the increase in net rate base is an increase in depreciation expense, insurance expense and an increase in property taxes associated with the increased value of the Company's rate base. During the three years since the Company's last rate case, depreciation, insurance and taxes other than income taxes have increased by $24 million, $1.5 million, and $5 million respectively.

Other expenses have also increased. The increased regulatory and legal complexity of the electric business, the need to begin hiring and training new employees in anticipation of the approaching retirement of many of the Company's most skilled and experienced workers and inflation in labor markets generally have resulted in increases in labor costs. These increases are reflected in the rate increase request. Similarly, although increases in SCE&G's healthcare costs have been lower than national averages for the reasons Mr. Marsh discusses, those costs have increased in absolute terms as a result of inflation and the fact that the Company has hired additional employees. As a result, increased health care costs are reflected in the increase request.

These are among the principal components underlying the need for rate relief at this time. This list is by no means comprehensive. In addition, the components putting upward pressure on rates are offset by increased revenues from new customers, and by other efficiencies and savings as discussed by Mr. Marsh. However, in aggregate, the factors increasing SCE&G's costs since the last rate case have predominated, and rate adjustments are required to maintain the Company's sound financial position.

Q. HOW DOES THE FINANCIAL COMMUNITY VIEW SCE&G AT THIS TIME?

A. The investment community is very much aware of SCE&G's capital expenditure plans related to the Company's expanding customer base, proposed environmental upgrades and construction of new nuclear capacity. The investment community also is aware that the Company will need to access national financial markets to generate the required capital. The question I hear consistently is: "How will the Company address these challenges while providing fair returns to investors?"

Q. HOW DOES THE BASE LOAD REVIEW ACT FIGURE INTO THESE CONCERNS?

A. The passage of the Base Load Review Act (the "Act") gave the financial community a strong signal of support from the General Assembly for SCE&G's nuclear construction plans. Through the annual rate revisions that the Act authorizes, the Company now has a clearly defined means to generate cash flow necessary to support the cost of financing new nuclear construction. In addition, the Act gives investors and the Company important assurances that prudency decisions made at the outset of construction process will not be second-guessed.

However, even with the Act, the Company is still at risk for meeting the pre-approved construction schedules and costs. Construction risks include those related to the cost and availability of skilled labor and specialty contractors, and those related to the increasing costs of construction materials like copper, steel, aluminum, and cement. For nuclear projects, construction risks also include regulatory risk. NRC regulations and policies are supportive of nuclear construction at this time; however, events that we cannot foresee could change that level of support during the eight to ten year construction period.

The Act offsets some of the additional financial and prudency risk the Company has incurred by moving forward to permit and build new nuclear capacity. But the Act cannot reduce the Company's risk profile to a point below where it was before it announced its intention to build new capacity. In short, the Base Load Review Act reduces but does not eliminate nuclear construction risk. That perception is widely shared in the financial community.

Q. WHAT BEARING DOES THIS CASE HAVE ON SCE&G'S ABILITY TO MANAGE THE RISKS OF NUCLEAR CONSTRUCTION?

A. As mentioned above, revised rates under the Base Load Review Act will provide an important part of the cash SCE&G needs to finance nuclear construction costs while construction is taking place. The Act provides that the ROE established in the applicant's most recent rate order can become the ROE that applies for rate revisions throughout construction of the plant –that is so long as the rate order was issued within five-years of the initial filing under the Act. As a result, the ROE established in this case could be the ROE under which the Company seeks to fund the cost of nuclear construction. The financial community understands that to be the case and will review the ROE granted here in that light.

In addition, nuclear construction is certainly one of the biggest single issues on the Company's horizon today. Investors are eager to gauge the level of regulatory support for the Company's construction plans and will review closely the order in this case for an indication about whether the Company has the Commission's support as it makes the key commitments related to that construction. Given the importance of ROE to future rate revisions under the Base Load Review Act, the ROE granted here will be evaluated closely for what it says – directly or indirectly – about the Company's ability to finance its nuclear and environmental construction obligations at reasonable rates in competitive capital markets.

Q. BASED ON YOUR EXPERIENCE WITH SCE&G AND THE CAPITAL MARKETS IN WHICH IT OPERATES, WHAT IS THE APPROPRIATE RATE OF RETURN ON EQUITY FOR SCE&G TODAY?

A. In my opinion, the appropriate return on equity on which the Commission should set rates in this case is 11.75%. My opinion that 11.75% is the fair and reasonable return on equity for SCE&G is based on my knowledge of the financial markets in which SCE&G operates, my understanding of the current expectations of those markets, and my understanding of how investors in those markets view SCE&G's risk profile. In my opinion, an 11.75% return on equity will meet investors' reasonable requirements given SCE&G's current risk profile. An ROE at this level should allow SCE&G to continue to attract capital on reasonable terms as it begins financing its planned investments in nuclear capacity while at the same time it responds to the robust growth in its service territory and invests substantial capital in environmental upgrades to its existing fossil fuel generation plants.

Q. PLEASE EXPLAIN WHY 11.75% IS THE FAIR AND REASONABLE RETURN ON EQUITY FOR SCE&G AT THIS TIME.

A. I agree with Dr. Murry's conclusion that the upper range of an ROE for the Company should be 12%. For example, I have reviewed the electric ROE awards given by the Commission in SCE&G's three electric rate cases prior to Order 2005-2. Those cases reflect the risks assumed by the Company in constructing the Cope Plant, in responding to pressures for retail deregulation during the mid-nineties, and in construction of the Jasper Plant. The average ROE granted in those cases was just below 12% -11.98% to be exact, and ROEs were granted as high as 12.45%. I think that the risks confronting SCE&G's electric business today are at least as great if not greater than the average risk during this prior period. I believe that the markets in which the Company competes for capital – characterized as they are today by hedge funds and private equity firms, increased global competition for capital, rising interest rates, and increasing concerns about inflation – are at least as competitive as they were on average during the earlier period.

In my opinion, a return on equity higher than 11.75% can be justified for SCE&G in today's conditions. However, I believe the Company can manage the financial challenges it confronts if the Commission grants it the opportunity to earn an ROE of 11.75%. On the other hand, while rate orders must be viewed as a whole, ROE is critical in this case. Too low a return could increase the risk that the Company will not be able to access capital markets on reasonable terms to support the construction of nuclear capacity and other capital needs. Downward departures from 11.75% increase the risk that the Company will not be able to convince investors that its plans for financing the costs of new nuclear generation are appropriate and workable.

As the courts have stated many times, the establishment of an ROE by this Commission is an exercise of judgment based on the facts presented and pragmatic considerations. In this proceeding, the importance of setting an ROE that meets investors' reasonable expectations is of paramount importance given the construction risks and capital spending obligations that the Company is preparing to undertake. The new nuclear capacity SCE&G is planning to permit and construct is of great importance to the State of South Carolina. This new capacity will serve not only SCE&G's customers but also the customers of its partner, Santee-Cooper, and of the electric cooperatives Santee-Cooper serves. All told, the nuclear capacity SCE&G plans to permit and build will serve approximately 1.3 million retail electric customers --or 56% of South Carolina's approximately 2.3 million electric customers.

Based on my judgment and my knowledge of the financial community, an ROE of 11.75% is a reasonable and pragmatic result in this case given the current risk profile and capital needs of the Company, and the importance to the State of the successful completion of the construction plan SCE&G is preparing to undertake.

Q. DO YOU HAVE ANY ADDITIONAL REQUESTS?

A. The Company is requesting the Commission extend until December 31, 2015 the period over which it would be able to apply the accelerated capital recovery mechanism originally approved by the Commission in Docket No. 1999-389-E, Order No. 1999-655. This Order allows the Company in its discretion to accelerate depreciation of its Cope Generating Station when revenue or expense levels warrant. The mechanism was extended by the Commission in Order 2003-38 and in then again in Order 2005-2. The current expiration date is December 31, 2010.

Should the Company experience a period of unusual levels of expenses or revenues, the mechanism created by Order No. 1999-655 will still be a useful tool for responding to such circumstances. Under the mechanism, the Commission maintains at all times the ability to initiate a rate reduction proceeding if it believes that the Company's earnings will be higher than established levels on a sustained basis. The policy reasons that justified Order 1999-665 when issued continue to be valid and justify its extension. The Company respectfully requests that the Commission extend the applicability to the mechanism until December 31, 2015

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes, it does.